

810-27-1-4-.17     Sales Factor: Sales Other Than Sales of Tangible Personal Property.

(a) *In General.* Section 40-27-1, Article IV.17 provides for the inclusion in the numerator of the sales factor of gross receipts from transactions other than sales of tangible personal property (including transactions with the United States Government); under this section, gross receipts are attributed to this state if the income producing activity which gave rise to the receipts is performed wholly within this state. Also, gross receipts are attributed to this state if, with respect to a particular item of income, the income producing activity is performed within and without this state but the greater proportion of the income producing activity is performed in this state, based on costs of performance.

(b) *Income Producing Activity: Defined.* The term "income producing activity" means the act or acts directly engaged in by the taxpayer for the ultimate purpose of obtaining gains or profit. Such activity does not include transactions and activities performed on behalf of a taxpayer, such as those conducted on its behalf by an independent contractor. Accordingly, income producing activity includes but is not limited to the following:

(1) The rendering of personal services by employees or the utilization of tangible and intangible property by the taxpayer in performing a service.

(2) The sale, rental, leasing, licensing or other use of real property.

(3) The rental, leasing, licensing or other use of tangible personal property.

(4) The sale, licensing or other use of intangible personal property.

(c) *Income Producing Activity: Business Situs.* The income producing activity is deemed performed at the situs of real, tangible and intangible personal property or the place where personal services are rendered. The situs of real and tangible personal property is the commercial domicile of the taxpayer unless the property has acquired a "business situs" elsewhere. "Business situs" is I. the place at which intangible personal property is employed as capital; or II. the place where the property is located if possession and control of the property is localized in connection with a trade or business so that substantial use or value attaches to the property. This rule shall not apply to the performance of construction contracts.

EXAMPLE: Taxpayer, a corporation whose principal business activity is the manufacture and sale of hot water heaters pledges bonds in this state as security for the payment of taxes incurred or to be incurred in connection with its business activities in this state. The property has a business situs in this state; therefore, interest income derived from such bonds is attributable to this state.

(d) *Costs of Performance: Defined.* The term "costs of performance" means direct costs determined in a manner consistent with generally accepted accounting principles and in accordance with accepted conditions or practices in the trade or business of the taxpayer.

(e) *Application.*

(1) *In General.* Receipts (other than from sales of tangible personal property) which do not constitute a principal source of business income and which such receipts are included in the denominator of the receipts factor are in this state if:

(A) the income producing activity is performed wholly within this state; or

(B) the income producing activity is performed both in and outside this state and a greater proportion of the income producing activity is performed in this state than in any other state, based on costs of performance.

(i) EXAMPLE: The taxpayer is engaged in the heavy construction business in which it uses cranes, tractors, and earth-moving vehicles. The taxpayer makes short-term rentals of the equipment when not needed on any project. The taxpayer rented some of the equipment to A for three weeks. The equipment was used by A for two weeks in this state and one week in State X. The taxpayer's direct costs in connection with the equipment during the rental period was \$500 each week. Accordingly, the greater proportion of such costs was incurred in this state. All of the rental receipts are business income and for purposes of the sales factor are included in the numerator for this state.

(ii) EXAMPLE: Taxpayer, whose commercial domicile is in this state, manufactures and sells industrial chemicals. Taxpayer owns patents on certain of its products. The taxpayer licensed the production of the chemicals in foreign countries in return for which the taxpayer receives royalties which constitute a relatively minor amount of its income. The royalties are business income and for purposes of the sales factor are included in the numerator for the state of the taxpayer's commercial domicile.

(2) *Special Rules.* The following are special rules for determining when receipts from the income producing activities described below which constitute a principal source of business income are in this state:

(A) Gross receipts from the sale, lease, rental or licensing of real property are in this state if the real property is located in this state.

(B) Gross receipts from the rental, lease, or licensing the use of or other use of tangible personal property are in this state if the property is located in this state during the entire period of rental, lease, license or other use. If the property is within and without this state during the rental, lease or licensing period, gross receipts attributable to this state shall be measured by the ratio which the time the property was physically

present or was used in this state bears to the total time or use of the property everywhere during that period.

EXAMPLE: Taxpayer is the owner of 10 railroad cars. During the year, the total of the days during which each railroad car was present in this state was 50 days. The receipts attributable to the use of each of the railroad cars in this state are a separate item of income and shall be determined as follows:

$$\frac{(10 \times 50) = 500}{3650} \times \text{Total Receipts} = \text{Receipts Attributable to this State}$$

(C) Gross receipts for the performance of personal services are attributable to this state to the extent that such services are performed in this state. If services are performed partly within and partly without this state, the gross receipts from the performance of such services shall be attributable to this state based upon the ratio which the time spent in performing the services in this state bears to the total time spent in performing the services everywhere. Time spent in performing services includes the amount of time expended in the performance of a contract or other obligation which gives rise to such gross receipts. Personal service not directly connected with the performance of the contract or other obligation, as for example time expended in negotiating the contract, is excluded from the computations.

(i) EXAMPLE: Taxpayer, a road show, gave theatrical performances at various locations in State X and in this state during the tax period. All gross receipts from performances given in this state are attributed to this state.

(ii) EXAMPLE: The taxpayer, a public opinion survey corporation, conducted a poll by means of its employees in State X and in this state for the sum of \$9,000. The project required 600 man-hours to obtain the basic data and prepare the survey report. Two hundred of the 600 man hours were expended in this state. The receipts attributable to this state are \$3,000.

$$\frac{200 \text{ man hours}}{600 \text{ man hours}} \times \$9,000 = \$3,000$$

(D) Gross receipts from intangible personal property shall be attributed to this state based upon the ratio which the total property and payroll factors in this state bears to the total of the property and payroll factors everywhere for the tax period.

(E) The provisions of this paragraph shall apply to sales other than sales of tangible personal property to the United States Government.

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Authority: 40-2A-7(a)(5) and 40-18-57

History: Filed with LRS March 22, 1994. Certification filed with LRS June 10, 1994, effective date July 15, 1994.

